

SMATV services, will likely foster additional growth in the SMATV industry. SMATV operators also have begun to bundle local and long distance residential telephone services, closed-circuit security monitoring, Internet access, voice mail, and paging services in order to increase their competitive position *vis-à-vis* cable and other MVPDs.¹³⁴

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The emergence and development of DBS and other significant competitors to cable means that programmers now have meaningful alternative outlets for distributing their product. The presence of these alternatives, and the fact that they are growing much more rapidly than cable, necessarily reduces any MSO's power to foreclose rivals or to obtain unfair concessions from programmers. As the Commission recently observed, "*[w]ith the growth of alternative MVPDs, network programmers gain alternative avenues for distribution of their products, thus reducing cable operators' market power or influence in the purchase and distribution of network programming.*"¹³⁵

b. AT&T-MediaOne will control far too few distribution outlets to engage in vertical foreclosure or exercise monopsony power

In analyzing the ability of an MSO to foreclose rival program services or to obtain anticompetitive concessions from programmers, the only relevant systems are those for which the MSO controls programming choices or buys programming. If an MSO cannot force a cable

¹³⁴ *Id.*

¹³⁵ Memorandum Opinion and Order on Reconsideration and Further Notice of Proposed Rulemaking, *In the Matter of Implementation of Section 11(c) of the Cable Television Consumer Protection and Competition Act of 1992 - Horizontal Ownership Limits*, 13 FCC Rcd. 14462, ¶ 80 (1998) ("*Further NPRM*") (emphasis added).

system to decline to carry a rival program service, then the system is irrelevant to that MSO's ability to pursue a vertical foreclosure strategy. Similarly, an MSO derives no power to force anticompetitive concessions from a programmer based on a cable system for which it does not purchase programming, even if the MSO has a minority interest in the system.

After the Merger, AT&T will be involved to some extent in the purchasing or selection of programming for cable systems with approximately 21,206,000 subscribers. This includes all the subscribers for the AT&T and MediaOne cable systems identified in the charts contained in Appendices A and B, with the exception of those for which AT&T does not currently, and will not post-Merger, purchase programming or participate in making programming choices – *i.e.*, Cablevision, the two AT&T-Time Warner joint ventures (Kansas City Cable Partners and Texas Cable Partners, L.P., and TWE).¹³⁶ Based on a conservatively low estimated total MVPD subscriber base of 79,600,000,¹³⁷ AT&T thus would purchasing programming or participate in making programming choices for 26.6 percent of current MVPD subscribers.

¹³⁶ Also, AT&T has subtracted 735,000 subscribers to account for systems that will be transferred to Comcast upon consummation of the Merger with MediaOne.

¹³⁷ *Tempo Authorization* ¶ 13. AT&T believes that using 79,600,000 MVPD subscribers is conservative. For example, Donaldson, Lufkin, Jenrette ("DLJ") recently estimated that there were 82,074,000 MVPD subscribers. See *Cablevision Blue Book, Volume IX*, at 10 (Summer/Fall 1999). Moreover, both the Commission and DLJ estimates are based on subscriber counts from last year, a significant fact given the growth rates for DBS and other non-cable MVPDs cited above. By way of example, consider that the Commission released its *Fifth Annual Competition Report* in December 1998, estimating 76.6 million MVPD subscribers, and only five months later, in the *Tempo Authorization*, adjusted that estimate to 79,600,000, an increase of three million subscribers.

Moreover, AT&T recently entered into three transactions that will further reduce its subscriber count: 1) the sale of its interest in Falcon Communications, L.P.; 2) the reduction below five percent of its interest in the cable systems currently owned by Bresnan Communications Co., Ltd. Partnership; and 3) the sale of its interests in certain cable systems to Cox Communications, Inc. When these transactions are completed, AT&T's subscriber count will be reduced to approximately 18,886,000 or only 23.7 percent of current MVPD subscribers. Similarly, Comcast, separate from the Comcast Exchange discussed above, has an option to acquire additional cable systems from AT&T. If Comcast exercises that option, then AT&T's percentage of MVPD subscribers would be even further reduced.

Even assuming that one could legitimately define a video programming input "market" limited to MVPDs – and, as discussed below, video programmers, in fact, have many other outlets for their products – there could be no conceivable monopsony power or vertical foreclosure concern at these levels. If AT&T refused to carry (or offered only anticompetitive purchase terms) to a video programmer, the programmer would still be able to obtain carriage on other cable systems serving "over 50 million subscribers, well over the threshold for national success."¹³⁸ AT&T has previously demonstrated that many programming services have had success with far fewer subscribers.¹³⁹ In fact, the Commission has recognized that networks can achieve long-term success with only 15 to 20 million subscribers.¹⁴⁰ The video programmer

¹³⁸ *Further NPRM* ¶ 45.

¹³⁹ *See* TCI Ownership Limit Comments at 75-78.

¹⁴⁰ *See Fourth Annual Video Competition Report* ¶¶ 155, 165. Also, in the Commission's closed captioning proceeding, new cable programmers noted that it is necessary to have 10 to 20 million subscribers in order to attract advertisers (one of the keys to long-term viability). *See Further*
(Continued . . .)

would also retain access to the nearly 10 million subscribers currently served by DBS providers that, as noted above are already among the largest video programming purchasers. Indeed, even current AT&T subscribers would remain up for grabs through DBS providers, whose ability to capture those subscribers (by offering better content) would only be enhanced by any anticompetitive conduct by AT&T directed at video programmers. On these facts, there is no credible basis to conclude that AT&T post-Merger could foreclose rival programming services or exercise monopsony power – real world video programmers simply have too many alternatives.

Indeed, Applicants are aware of no precedent in *any* industry finding monopsony power with respect to a firm that purchases only twenty-five percent of the output of a given product. Even in cases involving concerted action by unaffiliated purchasers (and thus raising the specter of the very conspiracies in restraint of trade that the antitrust laws were designed to discourage), the Department of Justice has effectively established a “safe harbor” against monopsony power challenges when the firms in question account for less than 35 percent of total purchases, disposing of such matters through routine “Business Review” letters.¹⁴¹ In the few

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NPRM ¶ 44 (citing comments of Outdoor Life Network, Speedvision Network, The Golf Channel, BET on Jazz, and America’s Health Network).

¹⁴¹ See, e.g., *Business Travel Contractors Corporation*, 1995 DOJBRL LEXIS 9 (July 14, 1995) (declining to challenge the plans of a Pennsylvania business travel corporation (“BTTC”) to form a joint buying group to negotiate domestic air travel fares, finding that “[s]o long as BTTC’s customers do not account for more than 35 percent of air travel purchases over any city-pair market, it is unlikely that BTTC would be able to exercise monopsony power to negotiate fares that are below competitive levels”); *IFA Shippers’ Association*, 1990 DOJBRL LEXIS 2 (April 1990); see also *Utilities Service Alliance*, 1996 DOJBRL LEXIS 4 (July 3, 1996) (the Department “would challenge the formation or operation of a shippers’ association that is likely to result in the exercise of power over freight rates in any relevant market (‘monopsony power’), but “[t]his is unlikely where the membership’s total projected shipments are less than 35 percent of the total transportation services supplied.”).

single firm monopsony cases, the courts have consistently found that even much higher shares raise no competitive concerns, particularly where, as here, the sellers are sophisticated, large corporations. For example, in *United States v. Syufy Enterprises*, the court affirmed a summary judgment rejection of claims that a movie theatre chain that, during the relevant period, controlled as much as 75 percent of the Las Vegas market for first-run films was exercising monopsony power over Hollywood film distributors.¹⁴² The same recognition that very high share is necessary to support any plausible claim is reflected in the vertical foreclosure cases as well (which have arisen primarily in the monopoly, not monopsony, context). *See, e.g., United States v. Aluminum Co. of America*, 148 F.2d 416, 424 (2d Cir. 1945) (“[I]t is doubtful whether sixty or sixty-four percent would be enough; and certainly thirty-three percent is not”).¹⁴³

Here, moreover, the approximately 25 percent share of current MVPD subscribers vastly overstates AT&T’s post-Merger position with respect to video programmers. The entities that provide the overwhelming amount of video programming are large, sophisticated corporations that exercise substantial selling power through their control of unique, highly differentiated products. The very existence of MSOs and other MVPDs depends on obtaining

¹⁴² 903 F.2d 659, 663-71 (9th Cir. 1990). *See also* Jacobson & Dorman, *Monopsony Revisited*, Antitrust Bulletin 165 (Spring 1992) (“[T]he evidence is strong that true monopsony power is rare and that net adverse effects on price and output from monopsony are even rarer”).

¹⁴³ *See also* *Arthur S. Langenderfer v. S. E. Johnson Co.*, 917 F.2d 1413, 1432 (6th Cir. 1991) (“[I]t would be rare indeed to find a firm with only 25 percent or 50 percent of the market could control price over any significant period.”); I Antitrust Law Developments (Third), 213-214 (1992) (citations omitted) (“A market share in excess of 70 percent is almost always deemed sufficient to support an inference of monopoly power, although that inference may be overcome by other evidence. In contrast, a market share of less than about 40 percent virtually precludes a finding of monopoly power”); Areeda and Hovenkamp, ANTITRUST LAW 548-549 (1992 Supp.) (“[T]here is substantial merit in a presumption that market shares below 50 or 60 percent do not constitute monopoly power.”).

programming that subscribers are willing to pay to receive. And now that over 95 percent of all television households have access to at least two to three competing MVPDs, cable systems must acquire the programming that their customers demand or they will lose subscribership to DBS and other competing MVPDs.¹⁴⁴ Nor are video programmers limited to selling their products to MVPDs. To the contrary, video programming service suppliers have many other outlets for their products, including broadcast, home video, and international markets.

Concerns that AT&T (or other MSOs) could impair the programming marketplace through vertical foreclosure are misplaced for additional reasons as well. Such conduct is already largely foreclosed by existing regulations, such as the program access, program carriage, must carry, leased access, and channel occupancy rules, which already prohibit discrimination and require the carriage of programming from diverse sources.¹⁴⁵ Further, it is important to recognize that TCI has previously supplied *empirical evidence* that it “does not favor affiliated programming services in any way that significantly forecloses non-affiliated programming.”¹⁴⁶ Finally, AT&T would have no incentive to attempt vertical foreclosure even if it had the ability

¹⁴⁴ *Tempo Authorization* ¶ 16. The substantial bargaining power that programmers enjoy by virtue of their exclusive control over popular programming networks and services is perhaps most aptly illustrated by the acceptance by even the largest cable MSOs of a 20 percent rate increase in the licensing fees charged by ESPN. Despite concerns that subscribers would not be willing to absorb this increase, the vast majority of large cable operators and cable MSOs retained ESPN. *See Id.* ¶ 174.

¹⁴⁵ The Commission has recognized that because these rules “all affect the way the cable television industry currently operates and have a profound effect on current industry structure and performance,” it is appropriate “to consider the impact of these provisions in alleviating some of the public interest and anticompetitive concerns about horizontal concentration.” *Further NPRM* ¶ 50. Moreover, these other behavioral restrictions have proven successful and, in some cases, have been strengthened since adoption of the suspended horizontal limit. *See TCI Ownership Limit Comments* at 21-25.

¹⁴⁶ Besen and Woodbury at A-1 *supra* n.101.

to do so. Any vertical foreclosure benefit to existing AT&T programming interests would not go to AT&T shareholders, but would go to Liberty shareholders. MediaOne's programming interests are virtually all minority interests, and thus, any gains to these new AT&T programming interests also would flow primarily to others. Yet AT&T would bear all of the substantial costs of the vertical foreclosure strategy – *i.e.*, reduced subscriber revenues that would flow from the reduced quality of its offerings occasioned by denying subscribers access to popular rival programming services.

In short, there is no basis for concluding that the Merger will give AT&T the ability to exercise monopsony power or to engage in vertical foreclosure.

3. The Commission's Suspended Horizontal Cable Ownership Rules, however they are Ultimately Resolved, should Not be an Obstacle to the Merger

AT&T recognizes that even beyond its competitive interest analysis, the Commission has an independent duty to assess the impact of a proposed transfer of control on the transferee's compliance with statutes and Commission regulations, including those addressing the ownership of cable systems. As the Commission is aware, however, the statutory cable horizontal ownership provision has been held unconstitutional,¹⁴⁷ and the Commission's cable horizontal ownership rule has been stayed.¹⁴⁸ Thus, the Merger currently would not result in a violation of the statute or the Commission's rule.

¹⁴⁷ *Daniels Cablevision, Inc. v. U.S.*, 835 F. Supp. 1 (D.D.C. 1993).

¹⁴⁸ *1993 Ownership Order* ¶ 10. The stay of the notification provisions of the horizontal rule has been lifted, and AT&T has been complying with those requirements.

AT&T understands, of course, that the decision finding the statutory horizontal ownership provision unconstitutional is under appeal and that the Commission has initiated the *Further NPRM* on the horizontal rules and a related *NPRM* on the cable attribution rules.¹⁴⁹ AT&T will comply with all Commission rules. Regardless of the Commission's approval of the Merger, AT&T acknowledges that it will be subject to the general rules established in the ongoing rulemaking proceeding that is the subject of reconsideration and appellate review. While AT&T has supported the proposition that the Merger will not have anticompetitive effects on video programming services,¹⁵⁰ if, under rules the Commission adopts, AT&T exceeds the permitted level of horizontal ownership, it will either obtain an appropriate waiver based on the benefits to competition that will not otherwise be achieved, or bring itself into compliance with the rules.

With regard to the suspended cable horizontal ownership limit, AT&T and MediaOne, in the ongoing proceedings in the various rulemakings, have maintained that the

¹⁴⁹ *Notice of Proposed Rulemaking, In the Matter of Implementation of the Cable Television Consumer Protection and Competition Act of 1992 - Review of the Commission's Cable Attribution Rules*, 13 FCC Rcd. 12990 (1998).

¹⁵⁰ Congress enacted the horizontal limit based on the concerns that cable operators could: (1) exercise monopsony power to force unfair concessions from programmers, *see* H.R. Rep. No. 102-628, at 42-43 (1992), and (2) vertically foreclose entry by programmers, thereby reducing program diversity. *See* S. Rep. No. 102-92, at 32 (1991). As the Commission has acknowledged, the purpose of the horizontal ownership limit relates entirely to the ability of cable operators to affect video programming. *See* Second Report and Order, *In the Matter of Implementation of Sections 11 and 13 of Cable Television Consumer Protection and Competition Act of 1992 - Vertical and Horizontal Ownership Limits*, 8 FCC Rcd. 8565, ¶ 10 (1993) ("1993 Cable Ownership Order") ("Congress concluded that [the] degree of [cable] concentration, though low relative to other industries, may enable some MSOs to exercise excessive market power, or monopsony power, in the program acquisition market. Congress was concerned in particular with preventing large vertically integrated cable systems from creating barriers to entry for new video programmers, and from causing a reduction in the number of media voices available to consumers.").

Commission should take the following approach: 1) consistent with the underlying purposes of the rules, attribute to an MSO only those cable systems for which the MSO controls programming choices or purchases programming; 2) consistent with the Commission's proposal in the *Further NPRM*, measure an MSO's horizontal concentration level as a percentage of all MVPD subscribers; and 3) for the reasons set forth in *TCI's* Horizontal Ownership Comments, significantly raise the 30 percent limit. Under this approach, as described above, AT&T would be involved in programming decisions or purchase programming for 26.6 percent (or 23.7 percent after the Falcon, Bresnan and Cox transactions close) of all MVPD subscribers nationwide.¹⁵¹

If the Commission instead were to consider AT&T's post-Merger horizontal concentration level on a cable homes-passed basis, then AT&T would be involved in programming decisions or purchase programming for cable systems with approximately

¹⁵¹ AT&T and MediaOne today do not, and AT&T post-Merger will not, control programming choices or purchase programming for: Cablevision (3,149,000 subscribers; 5,126,000 homes passed); the two AT&T-Time Warner cable joint ventures (1,416,000 subscribers; 2,686,000 homes passed); and TWE (9,734,000 subscribers; 15,254,000 homes passed – after subtracting the two AT&T-Time Warner joint ventures, which are otherwise included in the TWE numbers). As pointed out above, these systems should not be attributed to AT&T because they do not give AT&T any ability to engage in vertical foreclosure or exercise monopsony power. In any event, the homes passed numbers should not be used as a measure because they do not take into account other MVPD competitors. As the Commission itself has proposed, horizontal concentration should be measured by MVPD subscribers, rather than homes passed.

34,760,000 cable homes passed,¹⁵² or approximately 34.8 percent¹⁵³ of all cable homes passed. When the Falcon, Bresnan and Cox transactions are completed, AT&T will pass 31,015,000 cable homes, or approximately 31 percent of all cable homes-passed.

As shown above, market shares of this size are no cause for concern because they do not give firms the ability to engage in vertical foreclosure or to exercise monopsony power. Such a conclusion is consistent with Congress' decision in the 1996 Act to raise the national broadcast limit from 25 percent to 35 percent.¹⁵⁴ And, because the broadcast rules still allow for a discount for UHF stations, the effective horizontal limit for broadcasters is well above 35 percent.¹⁵⁵

¹⁵² This includes all the homes passed for the AT&T and MediaOne cable systems identified in the charts contained in the Appendices, with the exception of Cablevision, the two AT&T-Time Warner joint ventures, and TWE. In addition, AT&T has subtracted from these numbers 1,155,000 homes passed to account for a reduction in homes passed resulting from the Comcast Exchange. As noted, Comcast also has a separate option to acquire additional cable systems from AT&T. If Comcast exercises that option, AT&T's percentage of cable homes passed will be even further reduced.

¹⁵³ This percentage is calculated by dividing 34,760,000 by 100,000,000 cable homes passed. However, the number may be substantially in excess of 100,000,000. Although a Kagan estimate of 95,520,000 total cable homes passed is sometimes cited, that figure is not appropriate for use in measuring an MSO's percentage of cable homes passed. TCI previously submitted to the Commission a separate study *performed by Kagan* indicating that the 95,520,000 estimate is unreliable and that the number could be well in excess of 100,000,000. See Letter from Michael H. Hammer, Esq., Willkie Farr & Gallagher, to William F. Caton, Secretary, Federal Communications Commission, *Ex Parte* Presentation, MM Docket No. 92-264 (Oct. 9, 1997). In fact, AT&T believes that given the significant changes in the MVPD marketplace over the past six years since the rule was adopted, the Commission could not now enforce a cable homes-passed test even if the suspended rules were reinstated. For these reasons, and the other reasons set out in TCI's prior comments, AT&T strongly endorses the Commission's proposal in the *Further NPRM* to use an MVPD subscriber test. See TCI Ownership Limit Comments at 56-65.

¹⁵⁴ 1996 Act, Pub. L. NO. 104-104, § 202(c)(1), 110 Stat. 56,111 (1996).

¹⁵⁵ 47 C.F.R. § 73.3555(e)(2)(i). For example, both Paxon and Fox have an effective national reach above 40 percent before applying the Commission's 50 percent discount for UHF stations.

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Moreover, the cable homes-passed measure completely ignores the considerable increase in the number of subscribers served by competing MVPDs, most importantly DBS, so that it vastly overstates an MSO's ability to engage in vertical foreclosure or to exercise monopsony power. Thus, if the Commission were to retain a homes-passed approach, it at the very least would have to modify its present formula to take into account the established competition from non-cable MVPDs, discussed above, both at present and going forward – *i.e.*, it would have to adopt a self-adjusting formula that would automatically recalculate an MSO's share as MVPD competition increases or decreases. Of course, the Commission could avoid the complexities of such a modified homes-passed approach by adopting the proposal in its *Further NPRM* to implement an MVPD subscriber formula.

In addition, whether measured on a subscriber or homes-passed basis, there is no concern that the Merger will reduce program diversity. First, as noted, AT&T post-Merger will not have sufficient size to enable it to foreclose programming services and thereby limit diversity. Second, the growth of DBS and other non-cable MVPDs provides programmers with additional viable distribution options. Third, as the Commission has found, independent programming sources have increased rapidly, and program diversity is at an all-time high.¹⁵⁶

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Moreover, because LMAs are not attributable, the effective national reach of certain broadcasters is in the 60 percent range. *See TCI Ownership Limit Comments at 71-72.*

¹⁵⁶ For example, the number of national satellite services has increased from 106 in 1994 to 245 in 1998. During this same time, the percentage of programmers vertically integrated with cable has declined from 53 percent to 39 percent. *See Fourth Annual Video Competition Report* ¶ 158; *Fifth Annual Video Competition Report* ¶ 159. As the Commission recently found, over 70 national programming services unaffiliated with cable operators were planned to be launched in the near future, whereas only five national programming services affiliated with a cable operator were planned for launch. *See Fifth Annual Video Competition Report* at Tables F-3 and F-4.

Fourth, an MSO's ability to limit diversity by dictating content is substantially in check due to the Supreme Court's affirmance of the "must carry" rules in 1997. Finally, the emergence and widespread deployment of digital video technology by cable and non-cable MVPDs is increasing the number of programming outlets and creating additional incentives for the development of diverse new programming sources.¹⁵⁷

AT&T recognizes that the suspended horizontal ownership rules and the underlying attribution rules attribute to an MSO even small minority ownership interests in cable systems whether or not the MSO buys programming for the system or controls the system's programming choices. AT&T believes this is an unjustifiable and unsupportable approach because such minority interests do not confer the ability to control programming that is at the heart of the horizontal ownership limit.

It is particularly important that the Commission modify the approach taken in the suspended horizontal rules given the high priority Congress placed on the development of local, residential telephone competition in the 1996 Act. AT&T is the only company to step forward with a commitment (and the extraordinary capital investment) to provide expansive, facilities-based alternatives to the ILEC monopolies. AT&T has proven that it stands ready to offer the benefits of telephone competition – lower prices, improved customer service, and technology innovation – to consumers across the nation. In fact, as one financial analyst report recently stated: "Besides AT&T, no other company has yet laid out a coherent plan for attacking a broad swathe of the Bells' residential business."¹⁵⁸

¹⁵⁷ See also TCI Ownership Limit Comments at 21-44. —

¹⁵⁸ *New Communications Industry Takes Shape*, FT Telecoms, at p. 1 (June 9, 1999).

As discussed above in Sections IV and V(A), however, entering and competing in the local telephone business will be exceedingly difficult. The ILEC monopoly is over 100 years old, and the ILECs today still have virtually complete control over the residential subscribers in their territories. In addition, it is enormously expensive, technologically complicated, and labor intensive to upgrade cable systems to compete with the ILEC monopolies, and there is no guarantee that these investments will be successful. The Commission should not adopt cable horizontal rules that prevent AT&T from bringing local telephone choice to millions more consumers and from achieving the economies of scale and other benefits associated with large network size that are critical to providing alternatives to the ILEC monopolies.

The Commission has more than ample authority to adopt horizontal ownership rules that ensure that cable operators do not act anticompetitively in the programming marketplace, but at the same time encourage local telephone competition. In fact, the Communications Act compels such a balance. When Congress adopted the horizontal ownership provision in the 1992 Cable Act, it specifically instructed the Commission to take account of the fact that cable networks were evolving rapidly and had the potential to provide consumers with a vast array of new technologies and services.¹⁵⁹ When Congress spoke again in the 1996 Act, it emphasized most strongly the need to develop local telephony competition, and noted the unique role cable companies could play in developing such competition. The *only* way the Commission can harmonize the 1992 and 1996 Acts is to adopt cable horizontal rules that contain the

¹⁵⁹ For example, Congress mandated that the Commission “account for any efficiencies and other benefits that might be gained through increased ownership or control” of cable systems, 47 U.S.C. § 533(f)(2)(D), and that it adopt rules that “reflect the dynamic nature of the communications marketplace,” *id.* § 533(f)(2)(E).

minimum limitations necessary to protect an increasingly competitive video marketplace, but do not hamper the growth that is necessary to stimulate local telephony competition.

Finally, if the suspended horizontal rules are reinstated, and if the Commission does not amend the rules in a manner that results in AT&T's compliance with the rules as adopted, AT&T could seek a waiver of the rules. A waiver clearly would be appropriate in those circumstances where competitive harms are nonexistent and there are enormous countervailing benefits that cannot otherwise be achieved.

Given that the proposed transaction threatens none of the competitive harms that the statute and horizontal rules were designed to address, and that it promises enormous public interest benefits – indeed, the only short-term prospect for real local telephone competition for millions of Americans – the horizontal ownership rules should not pose an obstacle to the proposed Merger. This is especially true where, regardless of how the ownership limits are ultimately crafted, AT&T will bring itself into compliance: AT&T will comply with whatever ownership limits emerge from the current judicial and Commission proceedings.

G. Internet Services

Internet access services allow consumers to connect with the global “network of networks” that comprises the Internet and World Wide Web. These services are provided by companies that combine a range of features including connectivity to the Internet and, in many cases, proprietary content.

AT&T provides its WorldNet Internet access service to approximately 1.8 million customers, out of an estimated 33.7 million Internet users nationwide.¹⁶⁰ AT&T also holds a 25.9 percent equity interest and a 57.9 percent voting interest in At Home Corporation, which provides Internet access services. AT&T offers the @Home service to approximately 74,000 subscribers in connection with cable operations. After the Merger, AT&T will also hold approximately a 35 percent interest in Road Runner, which also provides Internet access services. Through its ownership of MediaOne, AT&T will provide the Road Runner service to approximately 125,000 customers.

The provision of Internet access services is already highly competitive. Internet service providers ("ISPs") compete for customers across a wide variety of features and options, including transmission speed, content, and customer service. Literally hundreds of firms – including America Online ("AOL") (with about 18 million subscribers), Microsoft, the Bell operating companies, major satellite companies (including Hughes, Loral, and Lockheed), and dozens of other wireline and wireless firms – compete to provide consumers access to the Internet and to proprietary content compiled or developed by them or their partners.¹⁶¹ In its 706

¹⁶⁰ According to numbers relied upon by the U.S. Department of Commerce, there are approximately 33.7 million Internet subscribers in the United States, although individual estimates of the market vary significantly from each other. See U.S. Department of Commerce, *The Emerging Digital Economy II* at 2 (June 1999) (citing <www.nua.ie/surveys>).

¹⁶¹ The number of competitors is substantial. See *ACLU v. Reno*, 929 F. Supp. 824, 832-33 (E.D. Pa. 1996) (noting that consumers have a wide variety of avenues available by which to access the Internet, including AOL, Compuserve, the Microsoft Network, and Prodigy). See also Leslie Walker, *Rivals Cede Throne to AOL*, Washington Post, April 8, 1999, at E1 (naming some of the 4,000 companies providing dial-up access to the Internet); Boardwatch Magazine's Directory of Internet Service Providers, 11th Ed. 1999 (listing over 5000 ISPs).

*NOI Report*¹⁶² and the order approving the AT&T-TCI merger just a few months ago, the Commission confirmed that “there are a large number of firms providing Internet access services in nearly all geographic markets in the United States, and these markets are quite competitive today.”¹⁶³

The Internet and online service business today is dominated by AOL, which serves almost 18 million of the total 33.7 million subscribers. By contrast, AT&T (through WorldNet and @Home) and MediaOne (through Road Runner) currently serve only 2 million and 125,000 subscribers, respectively. Current competitors are well-established, and new competitors are emerging regularly. Clearly, the broad range of choices available today demonstrates that the market is already extremely sensitive to the needs of consumers. Even focusing solely on Internet access services available over broadband facilities, there is no indication of potential anti-competitive effects. Consumers have an array of broadband choices, and these choices can be expanded easily by the entry of additional suppliers. In fact, the Commission has already found that “the preconditions for monopoly appear absent,”¹⁶⁴ and dozens of broadband competitors have entered the market even since that finding was made.

Importantly, the Merger will not have any effect on the ability of customers to access the Internet content of their choice. Concerns about the delivery of integrated cable Internet services are not merger-specific; in any case, such offerings promise numerous pro-competitive benefits to consumers. Because the Merger will enhance competition and create

¹⁶² 706 *NOI Report* ¶¶ 7, 98.

¹⁶³ *AT&T-TCI* ¶ 93.

¹⁶⁴ 706 *NOI Report* ¶ 48.

more “choice among video- and content- enriched high-speed Internet access services”¹⁶⁵ for consumers, it is demonstrably in the public interest.

1. The Internet Access Services Marketplace is Highly Competitive, and AT&T’s Investment in Cable Systems will Make it More So

Internet access service is a product comprised of inputs, each of which is available from a wide range of firms. As a threshold matter, consumers need both “connectivity” with the Internet and “transport” between their premises and the connectivity provider.¹⁶⁶ Consumers then use the Internet to access “content” made available on servers connected to the Internet.¹⁶⁷ Companies may offer these three components individually or in a variety of bundles, but to the consumer they are all part of one service: access to the Internet.¹⁶⁸ With respect to any given set of Internet consumers, the relevant geographic markets are local. However, because the same

¹⁶⁵ *AT&T-TCI* ¶ 147.

¹⁶⁶ The Commission has described Internet access as a combination of “computer processing, information storage, protocol conversion, and routing, with transmission,” which allows users to access Internet content and services. Universal Service Report to Congress, *Federal-State Joint Board on Universal Service*, 13 FCC Rcd. 11501, ¶ 63 (1998) (“*Universal Service Report to Congress*”). For purposes of this statement, this component will be referred to as “connectivity.”

¹⁶⁷ Content can include traditional text and graphic images, video, audio, and interactive services such as email and “chat.”

¹⁶⁸ The Commission has identified various “categories” of Internet services, yet noted that many companies fall into more than one of these categories. See *Universal Service Report to Congress* ¶ 62 (distinguishing between access providers, application providers, content providers, and backbone providers); B. Esbin, *Internet over Cable: Defining the Future in Terms of the Past* at 17 (FCC OPP Working Paper Series No. 30, 1998) (explaining that it “is still possible to differentiate ‘online service providers’ from ‘Internet service providers’ or ‘ISPs,’ although the distinctions have grown blurred in practice.”) (“*Internet Over Cable*”).

competitive conditions apply nationally, there is no need for separate analysis of any individual market.¹⁶⁹

The relevant market includes Internet access services available to consumers over both broadband and narrowband facilities.¹⁷⁰ Regardless of whether they rely on broadband or narrowband facilities, firms compete with each other to provide the combination of price, service, speed, and convenience best suited for each consumer. Broadband and narrowband services are priced competitively, each costing about forty dollars per month when a second phone line for dial-up access is factored in. The main advantage of broadband facilities over narrowband facilities is faster speeds. However, the array of applications tailored to the broadband environment is currently quite limited. Moreover, traditional dial-up services may also provide unique email or “chat” features that make them particularly attractive to consumers who value these capabilities.¹⁷¹ Consumers who use Internet services primarily for such email and “chat” functions have no need for faster download speeds. Moreover, narrowband access is “portable” – it can be used from any location accessible by a normal phone line – while broadband access is not.

¹⁶⁹ *Accord AT&T-TCI* (declining to analyze any specific local markets for Internet access services).

¹⁷⁰ Even if the Commission finds that broadband and narrowband services are in separate markets, it still should conclude there are no anticompetitive concerns. There is substantial competition and ongoing entry to provide broadband access services. *Accord, AT&T-TCI* ¶ 92 (finding no need to determine whether broadband and narrowband Internet access services are the same or two distinct product markets, because in either case the merger was unlikely to adversely affect the public interest).

¹⁷¹ Consumers who value such features will tend to “stick” to the service for a longer period of time before switching to an otherwise acceptable substitute.

Competitors themselves view narrowband and broadband services as substitutes for the foreseeable future. Many industry experts agree that Internet access over traditional phone lines shows no signs of diminishing in appeal. Even AOL's chief executive officer, Steve Case, has predicted that five years from now "seventy-five percent of the market will be narrowband because people want it to be as easy and inexpensive as possible."¹⁷² Other AOL executives have explained that the company is "technology agnostic"¹⁷³ and believes that broadband services will appeal primarily to consumers who are already online and want to upgrade to a faster connection.¹⁷⁴ AOL does not believe its millions of customers need access speeds much greater than 28.8 kpbs.¹⁷⁵ Prodigy Communications Corp. apparently has reached a similar conclusion, as demonstrated by its recent announcement that it would purchase Cable & Wireless's dial-up Internet access service in a deal worth up to \$75 million.¹⁷⁶

Clearly, the availability of narrowband alternatives will continue to discipline the price of services available over broadband facilities until those services can offer something beyond "faster" downloads. Because narrowband alternatives provide millions of consumers with the basic services they need, it is highly unlikely that even a "monopoly" provider of

¹⁷² See *Power Lunch*, Television Interview with Steve Case (CNBC broadcast, September 28, 1998).

¹⁷³ Ashley Dunn, *AT&T's Bold Move*, Los Angeles Times at C4 (May 6, 1999).

¹⁷⁴ Thomas E. Weber and Stephanie N. Mehta, *AOL Hopes to Trump Cable Deal by Using Some Fast Phone Lines*, Wall Street Journal (May 7, 1999).

¹⁷⁵ See Transcript of Panel Discussion, *Cyberspace and the American Dream*, Aspen Summit, (Aug. 25, 1998) (interview with George Vradenburg, AOL's Vice President for Law and Public Policy) ("Vradenburg Interview").

¹⁷⁶ Maura Ginty, *Prodigy to Buy Cable & Wireless U.S.A.'s Dial-Up Service*, InternetNews.com (May 27, 1999) <www.internetnews.com>.

broadband services would be able to raise prices profitably. All these factors demonstrate that broadband access is part of the overall Internet access services market.¹⁷⁷

Currently, there are “a large number of firms providing Internet access services in nearly all geographic markets in the United States, and these markets are quite competitive today.”¹⁷⁸ These firms employ different competitive strategies and offer different combinations of features to attract subscribers. There is no question that the market for Internet access services is “extremely competitive and highly fragmented,” with “no substantial barriers to entry.”¹⁷⁹ Even with respect to the broadband sector, the Commission reached the same conclusion only a few months ago, finding that there are “a large number of actual participants and potential entrants.”¹⁸⁰ In light of this intense competition, the Commission decided that no regulatory intervention on its part was required.¹⁸¹

¹⁷⁷ AT&T, @Home, and Road Runner also provide Internet backbone services, which route traffic between Internet access providers. See *MCI-WorldCom* ¶ 143 n.383 (describing backbone services). Nevertheless, the Merger will not create or enhance market power in the provision of backbone services because only AT&T owns its own facilities to provide these services. @Home and Road Runner each lease facilities from other backbone providers. In any case, even AT&T, @Home and Road Runner combined would have a *de minimis* share of any such “market.”

Likewise, while AT&T and MediaOne also provide Internet access services to business customers, there are many companies providing similar services and, after the Merger, AT&T will still only have a *de minimis* share of this business. Accord, *AT&T-TCI* ¶¶ 60-61 (considering only residential usage of Internet access services).

¹⁷⁸ *AT&T-TCI* ¶ 93. See also *706 NOI Report* ¶ 90 (according to one study, over 90 percent of the country has access by a local call to several Internet service providers).

¹⁷⁹ 1998 MindSpring Enterprises, Inc. 10-K at 18. See also 1998 America OnLine, Inc. 10-K at 17 (listing a wide range of competitors in the “rapidly-changing” marketplace).

¹⁸⁰ *706 NOI Report* ¶ 48.

¹⁸¹ *Id.* ¶¶ 100-101.

The wisdom of that decision has been borne out by developments in the Internet market since January 1999. For example, every day there are more and more broadband transport alternatives.¹⁸² In just the last few months, AOL has announced deals with several Bell companies to use DSL service to provide high-speed Internet access. AOL has also continued its “AOL Anywhere” strategy through alliances with manufacturers of set-top boxes and electronic organizers and the acquisition of the major provider of on-screen program guides.¹⁸³ In addition, Hughes Electronics Corp. announced that it will invest \$1.4 billion in a two-way broadband data satellite network, Spaceway, that will begin providing service in the United States by the year 2002;¹⁸⁴ Sprint and MCI announced deals to acquire wireless cable companies;¹⁸⁵ Nextel introduced the first Internet-ready wireless phone;¹⁸⁶ and several data CLECs have had wildly successful initial public offerings.¹⁸⁷ Because the number of broadband alternatives increases

¹⁸² The stable regulatory environment created by the Commission has given providers of Internet access – and the financial community supporting them – the confidence to make the necessary investments.

¹⁸³ See Stephen Buel, *‘AOL Anywhere’ Philosophy Is Wider Reach, Marketing Muscle*, Mercury News (Nov. 24, 1998) (describing AOL’s “relentless drive to extend its supremacy across computer-based communicating”); Paul Fahri and Mike Mills, *AOL Seeks Boost Via Phone, TV*, Washington Post (Dec. 8, 1998); Andrea Peterson, *AOL, 3Com Form Partnership to Let Users Get E-mail on Palm Organizers*, Wall Street Journal (June 23, 1999).

¹⁸⁴ *Hughes Invests \$1.4B in Network* (March 17, 1999) <www.mercurycenter.com/svtech/news/breaking/ap/docs/2496651.htm>.

¹⁸⁵ See Jason K. Krause, *Wireless Cable Makes a Surprise Comeback*, The Industry Standard, April 29, 1999 (describing MCI-WorldCom’s acquisition of CAI Wireless Systems and Sprint’s acquisition of People’s Choice TV and American Telecasting) <www.thestandard.net>.

¹⁸⁶ Sarah Schafer, *Nextel First With Net Ready Phone*, Washington Post, at E3 (June 9, 1999).

¹⁸⁷ *Covad Shares Surge After \$140 Million IPO Placed*, TR Daily, January 22, 1999; Corey Grice, *Rhythms Triples on First Day of Trading*, CNET News.com (Apr. 7, 1999) <www.news.com>. Microsoft recently announced a \$50 million deal with Rhythms, which also
(Continued . . .)

every day, there is no way to monopolize the Internet access market by bundling broadband “transport” with connectivity or content.

As described in more detail below, AT&T and MediaOne compete with a vast array of companies that utilize different combinations of transport, connectivity, and content to attract subscribers:

- Some companies provide only connectivity, or “pure” Internet access.
- Some combine connectivity with transport over their own facilities, while others offer a “bundle” that includes transport purchased from a third party.
- Some providers include proprietary and non-proprietary content in their bundle, while other companies offer only content.
- Cable operators, which have chosen to provide a seamless offering that includes high-speed transport, connectivity, and content, offer customers yet another option for accessing the Internet.

All of these different providers compete in one Internet access “market,” although they may offer different components or combinations of components to consumers.

ILECs. All of the ILECs offer Internet access services to their subscribers that include transport and content. For example, Bell Atlantic offers “Bell Atlantic.net,” a dial-up Internet access service at speeds up to 56 Kbps.¹⁸⁸ Bell Atlantic is also deploying DSL technology and using it to provide broadband Internet access service to its subscribers. Bell Atlantic has announced plans to make its “Infospeed DSL” service available to 8 million homes

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received another \$30 million from MCI WorldCom in January. *Microsoft makes its first DSL stake*, CNET News.com, March 17, 1999 <www.news.com>.

¹⁸⁸ See *Bell Atlantic.net for Home* <www.bellatlantic.net/home/banet/south>.

by the end of 1999 and 16 million homes by the end of 2000.¹⁸⁹ US WEST offers subscribers to its US WEST.net Internet access service a choice of transport either over standard phone lines or US WEST's "MegaBit" DSL service.¹⁹⁰ US WEST currently has 35,000 subscribers for its "MegaBit" services,¹⁹¹ which are offered in forty cities and are capable of reaching several million customers throughout US WEST's sixteen state region.¹⁹²

GTE and Southwestern Bell offer Internet access three different ways: dial-up access over standard phone lines, ISDN, or DSL.¹⁹³ SBC's DSL Internet access service is available to two million homes and SBC plans to increase its availability to 8.4 million homes by the end of 1999.¹⁹⁴ GTE has announced plans to offer its DSL services in approximately 300 central offices in 16 states, the nation's broadest deployment of ADSL technology, which will enable GTE to offer "end-to-end Internet solutions on a broader scale."¹⁹⁵ BellSouth offers its

¹⁸⁹ Corey Grice, *Price Cuts Raise Stakes in DSL Race*, CNET News.com, March 31, 1999, www.news.com.

¹⁹⁰ See *MegaBit Services - Internet Connection* <www.uswest.com/products/data/dsl/connection.html>.

¹⁹¹ John Borland, *US West Works on National DSL Strategy*, CNET News.com (May 21, 1999) <www.news.com>.

¹⁹² See *US WEST Company Profile* <www.uswest.com/com/insideusw/info.profile.html>.

¹⁹³ See, e.g., *SBC We Make It Easy* <www.public.swbell.net/home.html>; *GTE Products and Services* <www.gte.net/pands/residential/dsl.html>.

¹⁹⁴ See *America Online and SBC Communications to Offer High Speed Upgrade to AOL Members* (March 11, 1999) <www-db.aol.com/corp./news/press/view?release=579>.

¹⁹⁵ See *GTE to Offer Ultra-Fast Internet Access* <www.gte.com/AboutGTE/news/adsl041398.html>.

customers their choice of "FastAccess" ADSL service or "Internet access for less,"¹⁹⁶ while Ameritech offers both "Ameritech.net" dial-up and SpeedPath ADSL services.¹⁹⁷

CLECs. Competitive LECs generally provide the transport component of Internet access service, by itself or bundled with connectivity. For example, Sprint is now offering its Sprint ION high-speed Internet access and telephone service to consumers,¹⁹⁸ while NorthPoint Communications offers wholesale high speed DSL service to ISPs nationwide.¹⁹⁹ Concentric Network Corporation's interconnection agreement with NorthPoint allows Concentric to offer a high-speed Internet access service to small and medium size businesses, telecommuters, and residential subscribers.²⁰⁰ Covad Communications has a "Telesurfer" DSL transport service for consumers, which is available from several ISPs who bundle it with their Internet services.²⁰¹ A new "lite" version of DSL, which is not quite as fast but much easier to

¹⁹⁶ See *BellSouth Buzz* <www.bellsouth.net/cgi-bin>. BellSouth's DSL services will reach six million lines by September 1999. *BellSouth Launches High-Speed BellSouth.net FastAccess ADSL Internet Service in Memphis* (May 3, 1999) <www.bellsouthcorp.com/proactive/documents/render/26162.vtml>.

¹⁹⁷ See *Ameritech Home Products - Internet services* <www.ameritech.com/products/answer/data.html>.

¹⁹⁸ See *Sprint Launches ION Offer for Residential Customers*, TR Daily (June 21, 1999).

¹⁹⁹ See *Northpoint Communications Will Surpass Combined Bells' DSL Deployment* <www.northpointdsl.com/about/press_981215a.html>; see *NorthPoint Communications: Partners Resources* <www.northpointdsl.com/partners2/index.html>.

²⁰⁰ See <www.concentric.net/corporate_info/about_concentric.html>.

²⁰¹ See <www.covad.com/partners>.

install, is viewed by Northpoint and Covad as a way to accelerate the deployment of high-speed access to consumers.²⁰²

Wireless. Fixed wireless services also provide the transport component of Internet access services. According to one industry analyst, “[w]ireless broadband provides firms an excellent way to deliver the last mile of Internet access.”²⁰³ For example, Teligent, which uses microwave signals to offer local phone and Internet services to small and medium businesses, has launched service in 23 markets and plans to offer service in 17 more by the end of 1999.²⁰⁴ Sprint and MCI-WorldCom recently acquired several wireless cable licensees, including People’s Choice TV, American Telecasting, and CAI Wireless,²⁰⁵ whose spectrum is wide enough to carry high-speed services. Sprint plans to use wireless cable technology to provide transport for its bundled offerings of voice and broadband Internet access services to consumers.²⁰⁶ MCI-WorldCom and Vulcan Ventures recently invested \$300 million dollars each in Metrocom Inc., which provides “last mile” wireless Internet access at 128 kilobits per second

²⁰² Jon Healey, *High-Speed Internet Access Gets a Boost*, San Jose Mercury News (June 22, 1999).

²⁰³ Phil Harvey, *Waking Up to Fixed Wireless*, www.UpsideToday.com (June 4, 1999) <www.upside.com>.

²⁰⁴ Corey Grice, *Short Take: Teligent Expands into Four New Markets*, CNET News.com (Feb. 8, 1999) <www.news.com>.

²⁰⁵ John Borland, *Wireless Cable Bidding War Ahead?*, CNET News.com (June 17, 1999) <www.news.com>; Jason Krause, *Wireless Cable Makes a Surprise Comeback* (April 29, 1999) <www.the-standard.net/articles/display/0,1449,4412,00.html?home.tf>.

²⁰⁶ John Borland, *Sprint Readies ION for Consumer Market*, CNET News.com (April 12, 1999) <www.news.com>.